Department of Education

HISTORICALLY BLACK COLLEGE AND UNIVERSITY CAPITAL FINANCING PROGRAM ACCOUNT

Fiscal Year 2008 Budget Request

CONTENTS

HISTORICALLY BLACK COLLEGE AND UNIVERSITY
CAPITAL FINANCING PROGRAM ACCOUNT

For administrative expenses to carry out the Historically Black College and University Capital Financing Program entered into pursuant to title III, part D of the Higher Education Act of 1965, as amended, $188,000. [1]

NOTES

A regular 2007 appropriation for this account had not been enacted at the time the budget was prepared; therefore, this account is operating under a continuing resolution (P.L. 109-289, Division B, as amended). The amounts included for 2007 in this budget reflect the levels provided by the continuing resolution.

Each language provision that is followed by a footnote reference is explained in the Analysis of Language Provisions and Changes document which follows the appropriation language.

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Analysis of Language Provisions and Changes

Language Provision	Explanation
[1] For administrative expenses to carry out the Historically Black College and University Capital Financing Program entered into pursuant to title III, part D of the Higher Education Act of 1965, as amended, $188,000.	In accordance with the Federal Credit Reform Act of 1990, this language appropriates funds to service existing loan obligations made under the HBCU Capital Financing program authorized under title III, part D of the Higher Education Act of 1965 (HEA). Because the statutory limitation on loans will be reached in 2007, no new loans will be made in 2008.

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Amounts Available for Obligation
($000s)

	2006	2007	2008
Discretionary appropriation:			
Appropriation, definite	$210	0	$188
Appropriation, indefinite	0	$178,929	0
Across-the-board reduction	-2	0	0
CR annual rate	0	$167	0
Subtotal, discretionary appropriation	208	179,096	188
Mandatory appropriation:	0	14,154	0
Subtotal, discretionary and mandatory appropriation	208	193,250	188
Unobligated balance expiring	-41	0	0
Total, direct obligations	167	193,250	188

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Obligations by Object Classification
($000s)

		2006	2007	2008
11.10	Full-time permanent	$133	$124	$128
11.52	Awards	3	3	3
12.00	Benefits	25	29	31
	Subtotal, personnel	161	156	162
23.10	Rent to GSA	4	4	4
25.21	Other services	0	4	17
25.72	Information technology................	2	2	4
26.00	Supplies	0	1	1
41.02	Subsidies for credit program	0	193,083	0
	Total	167	193,250	188

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Summary of Changes
($000s)

2007	$193,250
2008	188
Net change	-193,062

	2007 base	Change from base
Increases:		
Built-in:		
Increase in personnel compensation for annualization of the 2.2 percent FY 2007 pay raise and annualization of the predicted 3 percent FY 2008 pay raise	$124	+$4
Increase in the Department's share of health, retirement, and other benefits due to inflation	29	+2
Program:		
Increase in other services due to changing central support needs.	4	+13
Increase in information technology costs	2	+2
Subtotal, increases		+21
Decreases:		
Built-in:		
Decrease in credit subsidy because the re-estimate for the FY 2008 budget is executed at the end of FY 2007	193,083	-193,083
Net change		-193,062

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Authorizing Legislation

($000s)

Activity	2007 Authorized	2007 Estimate	2008 Authorized	2008 Request
Federal administration *(Federal Credit Reform Act of 1990, section 505(e) and title III, part D, of HEA)*	Indefinite	$167	Indefinite	$188
Hurricane loan subsidies *(Title II, chapter 6, section 2601, of the Emergency Supplemental Appropriations Act for Defense, the Global War on Terror, and Hurricane Recovery (P.L. 109-234))*	Indefinite[1]	193,083	0	0
Total definite authorization				
Total appropriation		193,250		188

[1] Title II, chapter 6, section 2601, of P.L. 109-234 provides an indefinite appropriation for the subsidy costs of the HBCU Capital Financing hurricane recovery loans authorized therein. The authority for these loans extends for 1 year after enactment of P.L. 109-234, from June 16, 2006 through June 15, 2007.

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Appropriations History
($000s)

	Budget Estimate to Congress	House Allowance	Senate Allowance	Appropriation
1999	$96	$196	$96	$96
2000	207	96	207	207
2001	208	207	208	208
2002	208	208	208	208
2003	211	208	208	207
2004	210	210	210	209
2005	212	212	212	210
2006	210	210	210	208
Supplemental (2007)	0	0	0	193,083
2007	190			167[1]
2008	188			

[1] A regular 2007 appropriation for this account had not been enacted at the time the budget was prepared; therefore, this account is operating under a continuing resolution (P.L. 109-289, Division B, as amended). The amounts included for 2007 in this budget reflect the levels provided by the continuing resolution.

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Federal administration
(Federal Credit Reform Act of 1990, section 505(e)
and the Higher Education Act of 1965, title III, part D)

FY 2008 Authorization ($000s): Indefinite

Budget Authority ($000s):

	2007	2008	Change
Personnel costs	$156	$162	+$6
Non-personnel costs	11	26	+15
Hurricane loan subsidies[1]	193,083	0	-193,083
Total	193,250	188	-193,062
Full-time equivalent employee	1	1	0

[1] The authority to make Hurricane recovery loans, which is provided in title II, chapter 6, section 2601, of P.L. 109-324, expires June 15, 2007.

PROGRAM DESCRIPTION

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Funds for this activity pay the Federal costs for administering the Historically Black Colleges and Universities (HBCU) Capital Financing Program. Since fiscal year 1996, this program has provided HBCUs with access to capital financing for the repair, renovation, and, in exceptional circumstances, construction or acquisition of educational facilities, instructional equipment, research instrumentation, and physical infrastructure.

HBCUs, which have played a prominent role in our Nation's history, have significant needs for capital improvements. However, in most cases these institutions cannot access traditional funding sources at reasonable interest rates. The HBCU Capital Financing Program supports the Department's goal to strengthen HBCUs by ensuring that HBCUs have access to low-cost financing to fund infrastructure improvements. This program has made low interest loans available for capital improvements to some of the Nation's most vulnerable institutions of higher education, which has allowed these institutions to make improvements to their capital stock, especially academic facilities and student living-quarters. Under this program, the Department is authorized to provide financial insurance to guarantee up to $375 million in loans and interest to qualifying HBCUs—$250 million for private HBCUs and $125 million for public HBCUs. To limit the Federal Government's exposure to incurring losses due to defaults and delinquencies, 5 percent of all loans are deposited in a mandatory, pooled escrow account from which loan payments can be made in the event of defaults or delinquencies.

The HBCU Capital Financing Advisory Board, appointed by the Secretary, advises the Secretary and the Designated Bonding Authority (DBA) as to the most effective and efficient

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means of implementing the program. The DBA, also selected by the Secretary, provides for the operation of the HBCU Capital Financing Program, which includes raising bond capital, making loans to eligible institutions, charging interest, and providing for a schedule of repayments. Direct loans are financed through the Federal Financing Bank and guaranteed loans are financed through the private market, with all loan payments fully insured by the Federal Government.

The administrative costs for this program include the personnel compensation and benefits for 1 full-time equivalent (FTE) employee, overhead, and other administrative services. The FTE reported in this account reflects the Department's estimate of the staff time devoted to administering the program. This estimate does not include FTE associated with the Department's centralized services, which are reflected in the Program Administration account in the Salaries and Expenses Overview. The major non-personnel costs include support for the HBCU Capital Financing Advisory Board and a contract with the DBA to provide technical assistance workshops.

Funding levels for the past 5 fiscal years were:

	($000s)
2003	$207
2004	209
2005	210
2006	208
2007	193,250

Subsidy Expense

In the first 10 years that the HBCU Capital Financing Program operated there were no delinquencies or defaults. The rigorous application and credit review process imposed by the Department and the DBA was credited with ensuring that institutions receiving loans under this program had the ability to comply with the terms of their loans. However, in 2004 Barber Scotia College lost its accreditation with the Southern Association of Colleges and Schools. As a result, students enrolled at Barber Scotia College were no longer eligible for Federal student assistance. With approximately 90 percent of the College’s students receiving some form of government assistance, this has rendered the College unable to service its debt under the program. Barber Scotia College has one $7 million loan under the program, of which $6,964,340 has been disbursed. When capitalized interest is included, there is a total of $7,209,907 currently outstanding. In addition, there will be a total of $5,656,491 in interest due over the remaining life of the loan. Since March 2005, Barber Scotia College’s principal and interest payments have been made out of the pooled escrow account. If Barber Scotia College’s payments continue to be drawn out of the pooled escrow account, it is estimated that, without additional funds, the escrow account will be able to maintain Barber Scotia College’s payments until the year 2014.

The Department has worked with OMB to reexamine the appropriateness of the cash-flow assumptions for the program, especially the default assumptions, in light of the program’s first default. Previously, the default estimate was calculated based on prevailing market-based rates. The Department has now re-calculated the default assumptions based on individual

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assessments of risk and potential recovery for each loan. In light of these new assumptions, the credit subsidy for the program, previously estimated at zero, was upwardly re-estimated to $14.1 million for loans already made. Furthermore, the Department now does not believe that the funds set aside in the program's escrow account would be enough to cover defaults and, as such, the program can no longer be considered a zero subsidy program, according to the terms of the Federal Credit Reform Act of 1990. In order for the program to be able to make additional loan guarantees in future years, specific budget authority would have to be provided through appropriations language. The Administration projects that the program will surpass the statutory loan cap in 2007 and thus does not propose to make additional loan guarantees in fiscal year 2008. Therefore the Administration has not requested such authority for 2008.

Hurricane Relief Loans

In fiscal year 2006, Congress passed the Emergency Supplemental Appropriations Act for Defense, the Global War on Terror, and Hurricane Recovery (P.L. 109-234). Section 2601 of this act created a new sub-program within the HBCU Capital Financing Program that would provide loans on advantageous terms to HBCUs affected by Hurricanes Rita and Katrina. Under this sub-program, the interest rate charged on loans is capped at 1 percent, fees associated with the program are less than those associated with the rest of the program, and institutions are not required to participate in the program's pooled escrow account. In addition, principal and interest payments on loans already made to affected HBCUs are deferred for up to 3 years, with the Department making any payments that come due during this period. The statute gives the Department authority to make loans under the new sub-program in excess of the overall program loan caps. The Department expects that three loans will be made under the new sub-program and has assumed one default and no recoveries in making initial subsidy estimates. In light of these forecast assumptions and the expected cashflows for the new sub-program, the Department's cashflow analysis estimates the subsidy rate for the program to be 76.21 percent. The authority to make hurricane recovery loans expires on June 15, 2007.

The initial subsidy estimate for the sub-program was $15.4 million. This estimate assumed three loans averaging $8 million. In working with the affected HBCUs since the legislation was passed, the Department has developed a better picture of the existing need and, using data developed by the DBA, now estimates that the actual loans will be significantly larger than the initial estimate assumed, in the range of $235 million. At this loan volume, the necessary credit subsidy would be approximately $179 million. As the program is developed and better information becomes available, the underlying forecast assumptions and the subsidy estimates will be revised.

In light of these expectations, the Department projects that the overall program will surpass the statutory loan cap of $375 million in principal and accrued interest in fiscal year 2007 at which point the Department will not have authority to make additional loan guarantees through the program in future years.

FY 2008 BUDGET REQUEST

For fiscal year 2008, the Administration requests $188,000 to support the administration of the Historically Black College and University (HBCU) Capital Financing Program. The request

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includes an increase of $6,000 needed to cover authorized Federal salary increases. The request also includes an increase of $15,000 for non-personnel costs that reflects an assessment of the contract needs for the programs in fiscal year 2008. Notably, the amount requested for contracts is still $70,000 less than the amount appropriated and expended in fiscal year 2004 for this purpose.

For presentation purposes, the administrative costs and full-time equivalent financed by this account are also included under the justification materials in the Salaries and Expenses Overview.

PROGRAM OUTPUT MEASURES **($000s)**

	2006[1]	2007[1]	2008
HBCU Capital Financing Program Loans			
Number of new loans:			
Private HBCUs	0	2	0
Public HBCUs	1	1	0
Total	1	3	0
New loan volume:			
Private HBCUs	0	$40,000	0
Public HBCUs	$15,264	$35,000	0
Total	$15,264	$75,000	0
Hurricane Relief Loans[2]			
Number of new loans:			
Private HBCUs	0	2	0
Public HBCUs	0	1	0
Total	0	3	0
New loan volume:			
Private HBCUs	0	$155,000	0
Public HBCUs	0	$80,000	0
Total	0	$235,000	0
All Loans			
Total number of loans:			
Private HBCUs	18	22	22
Public HBCUs	6	8	8
Total[1]	24	30	30

[1] All loans made to date are direct loans financed through the Federal Financing Bank.

[2] These data reflect the three loans expected to be made in fiscal year 2007 as a result of the new sub-program authorized in P.L. 109-234 for HBCUs affected by Hurricanes Katrina and Rita.

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PROGRAM OUTPUT MEASURES ($000s)

	2006[1]	2007[1]	2008
All Loans (continued)			
Total loan volume:			
Private HBCUs	$143,297	$418,297	$418,297
Public HBCUs	$72,114	$107,114	$107,114
Total	$215,411	$525,411	$525,411

1 All loans made to date are direct loans financed through the Federal Financing Bank.

PROGRAM PERFORMANCE INFORMATION

Performance Measures

This section presents program performance information. The Department has not yet developed performance measures for the program. One potential measure would be the estimated cost to the Federal government per $1 made in loan guarantees, compared to the benefit generated by the Federal investment. Another potential measure would be the length of time between the receipt of a pre-application and the final closing of a loan for each loan cohort. Timely processing is a good measure of the program's efficiency since any extensive delay can affect project costs.

Other Performance Information

Barber Scotia College's default and the subsequent drawing of funds from the shared escrow account have had a negative effect on the program, making HBCUs reluctant to take out additional loans from the program as long as 5 percent of their disbursements will be used to service the debt of another school. As a result, the demand for loans under the program dropped significantly in fiscal year 2006. The DBA, which holds the loans that are guaranteed through this program, is initiating foreclosure actions against Barber Scotia College to recover funds owed. It is expected that initiating such action would result in an increase in the demand for loans through the program.

In 2006, the U.S. Government Accountability Office (GAO) conducted an examination of the HBCU Capital Financing Program. The objectives of the study were to review: (1) HBCU capital project needs and program utilization, (2) program advantages compared to other sources of funds and schools' views on loan terms, (3) the Department's program management, and (4) new loan provisions specifically authorized by in June 2006 to assist in hurricane recovery efforts. GAO noted in the report that HBCUs have extensive and diverse capital project needs and that the HBCU Capital Financing Program provides them with access to low-cost capital financing and flexibilities not available elsewhere. The report also noted that the Department had taken steps to improve the program that included increasing flexibility by providing schools with both fixed and variable interest rate options, allowing for larger loans, affording schools with more opportunities to negotiate loan terms, and increasing marketing efforts for the program. The report also noted specific weaknesses in the Department's management of the program.

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GAO's recommendations are presented below, followed by a description of the Department's corrective actions.

- *The Department should regularly convene and consult with the HBCU Capital Financing Program's Advisory Board. Additionally, the Department and the Advisory Board should consider the feasibility of alternatives to the escrow arrangement. If the Department determines that statutory changes are needed to implement more effective alternatives, it should seek such changes from Congress.* The Department is committed to meeting with the HBCU Capital Financing Program's Advisory Board twice each year. An Advisory Board meeting was held on October 27, 2006, and the Department will hold another meeting with the Advisory Board during the spring of 2007. The meetings provide an opportunity for the Department and the Advisory Board to discuss a wide variety of topics.

- *The Department should enhance communication with HBCU Capital Financing Program participants by (1) developing guidance for HBCUs, based on other schools' experiences with the program, on steps that applicants can take to expedite loan processing and receipt of loan proceeds, and (2) regularly informing program applicants of the status of their loan applications and Department decisions.* The Department will take several steps to address this recommendation. Experiences of past borrowers will be studied to determine realistic time projections for each phase of the loan process and to identify lessons learned that could be shared with new applicants. The Department will develop a "Tip Sheet" for new borrowers that includes an overview of the loan process, a listing of documents commonly needed to process a loan, and information about how to expedite the loan application and closing processes. Further, the Department will develop a customer satisfaction survey that will be sent to borrowers 15 days after they have closed on a loan. Finally, the Department will implement processes to provide schools with clear and timely information using multiple forms of communication.

- *The Department should change its requirement that borrowers make monthly payments to a semiannual payment requirement.* While the Department understands institutions' preference for semi-annual rather than monthly payments, the potential for default, as well as each institution's potential exposure from the default of another program participant, leads the Department to believe that it would be imprudent to implement a less frequent payment schedule.

- *The Department should ensure that program subsidy cost estimation process include as a cash flow to the government the surcharge assessed by the FFB and paid by HBCU borrowers and pay such amount to the program's financing account. Additionally, the Department should audit the surcharge funds held by the DBA.* The Department is in the process of revising its fiscal procedures to ensure that fees are accurately collected and recorded, and is working to have the FFB fee transferred to the Department in a way that will continually account for FFB fees separately as they apply to each loan. Additionally, the Department has worked with the Office of Management and Budget to incorporate the fee into the Department's cash flow model for the program. Further, plans are underway to retain an independent firm to audit the DBA during fiscal year 2007, to assess the handling of loan funds and associated fees.

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- *The Department should increase monitoring of the DBA to ensure compliance with contractual requirements and ensure properly marketing the program.* The independent audit will assess the DBA's record-keeping function and determine documents the DBA needs to obtain to complete its files. The Department will ensure that each borrower's file is complete. Further, the Department now requires the DBA to submit quarterly reports on the status of program participation and financing, as well as a marketing report that includes activities tabulated by institutions' student enrollments, types, and locations. These new reporting requirements will be fully implemented in 2007.